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Inter-company trade acceptances

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be charged with current expenses in order to build up a large surplus which may be used for dividends. However, that is what has been done in the case at hand.

The resulting balance sheet is very misleading. Since the process of arriving at the amount shown as the balance in the capital reserve is shown in the statement, what has occurred is clear enough to any one versed in the subject. The danger lies in the fact that a large number of those who have occasion to read the balance sheet, particularly stockholders, have little or no knowledge of accounting. They may be led to believe that the entire \$5,500,000

shown as surplus is free for dividends, and they may buy stock on that assumption.

Such a statement of the matter could arise only from gross ignorance of the nature of capital stock without par value, or from an intent to mislead. Because of the comparative recency of capital stock without par value, there is much misunderstanding concerning its nature. The various state laws on the subject lack uniformity, and many are in an experimental stage. It is to be hoped that in the next few years progress will be made in clearing up the matter.

Inter-Company Trade Acceptances

THE certified public accountant, by virtue of the nature of his calling, serves more than one master. He has a responsibility to his client, to conserve his interests and to meet his wishes in so far as possible. He has an obligation to lenders and investors, to state the results of his investigations in such a way that the results may be relied upon. He has a duty to the general public, to assist in obtaining the maximum efficiency in industry.

To serve all equally well, and to prepare a report that is fair to all, at times is a difficult task. Occasionally a client desires that certain facts be suppressed, or be stated in a certain way, in order to make things look "rosy." More often than not, this desire is not the result of an intent to be deceptive, but of an inclination to be over-optimistic. On the other hand, lenders and investors are eager for a plain statement of all the facts, unfavorable as well as favorable. The aim of the accountant should be to prepare a statement which sets forth clearly all the important facts, and in so doing to conform as nearly to the wishes of his client as it will allow.

The application of this principle is illustrated by reports which accountants recently were called upon to prepare for a corporation and its subsidiary. The parent company was engaged in the manufacture

of a staple commodity. The subsidiary had been incorporated to take over and develop one line of the parent company's product. Its common stock was entirely owned by the parent company, and it was financed almost wholly by the latter.

A large part of the financing was done through the use of trade acceptances, which the parent company drew on the subsidiary for advances of cash and materials. The parent company in turn discounted these trade acceptances at the bank, and thus reimbursed itself.

Accountants were engaged to make an audit of the two companies, and to prepare a report to be submitted to banks for credit purposes. The president of the companies, who believed firmly in the soundness of his enterprises, desired to make as favorable a showing as possible. Since the subsidiary's financial condition was extremely weak, he desired that separate reports be rendered on the two companies, in order to avoid combining the unfavorable position of the subsidiary with the more favorable situation of the parent company in a consolidated report. The parent company was to do the borrowing, and its report only was to be submitted to banks.

The accountants acceded to this desire. A balance sheet of the subsidiary was

shown, however, as a schedule supporting the balance sheet of the parent company.

At this time there were about a half million dollars in trade acceptances which had been issued by the subsidiary to the parent company, and discounted by the latter at banks. These were shown as a liability in the subsidiary's balance sheet, although no indication was given as to whom the liability existed. In the parent company's balance sheet all notes and trade acceptances discounted were omitted from the assets and liabilities. A footnote was appended to cover the situation, explaining that the balance sheet did not include notes and trade acceptances discounted, in a certain amount, nor the contingent liability therefor. No mention was made, however, either in the balance sheet or in the comments, of the fact that the bulk of this amount consisted of obligations of the subsidiary company.

The attention of the accountants later was drawn to the fact that the statement was incomplete. In view of the financial position of the subsidiary, it was almost certain that the parent company would be forced to meet some of the subsidiary's obligations when they matured. However, no indication was given as to this contingency in the parent company's balance sheet, even though it was especially significant in view of large advances made by the parent company to the subsidiary on current account.

This is a case where accountants went too far in endeavoring to please their client. Although the client's wishes should be acceded to whenever possible, accountants should be most careful to see that no omission or distortion of important facts is permitted, which might result in a misleading statement, and subject them to severe criticism, if not financial liability.

Annual Meeting

THE 1925 annual meeting of members and managers was held at the executive offices on September 17, 18, and 19. The program differed somewhat from previous years, in that the entire first day was given over to informal gathering, which afforded an opportunity for many individual conferences and discussions. The change proved very welcome, since in previous years not enough time has been allowed for this sort of thing.

Another variation from the usual order consisted in holding the golf tournament on the second day, due to the fact that it is not possible to entertain visitors at a golf course on Saturdays and Sundays. The golf tournament has come to be an institution, and is an event to which every one looks forward with a great deal of pleasure, even though it may be followed with personal disappointment in some instances when the scores are recorded.

The prizes were awarded to the following:

Mr. Morris—Low gross

Mr. Jumonville—Low net

Mr. R. W. Peters—Consolation

The third day, Saturday, was given over to professional and business conferences, with Mr. Ludlam presiding at the meetings. Matters relating to practice office management and general administration were discussed first, after which considerable time was devoted to the subject of technical procedure.

Mr. Wildman announced that the second section of the technical procedure manual, which deals with the verification of cash records, is expected to be distributed by about October 15th. He then discussed at some length the method of approach to this subject in the manual, particularly with respect to the classification of situations with which we are confronted in auditing, the variations calling for differences in auditing procedure. He pointed out that the studies which have been conducted by the technical procedure department on the possibilities of perpetration and concealment of fraud,